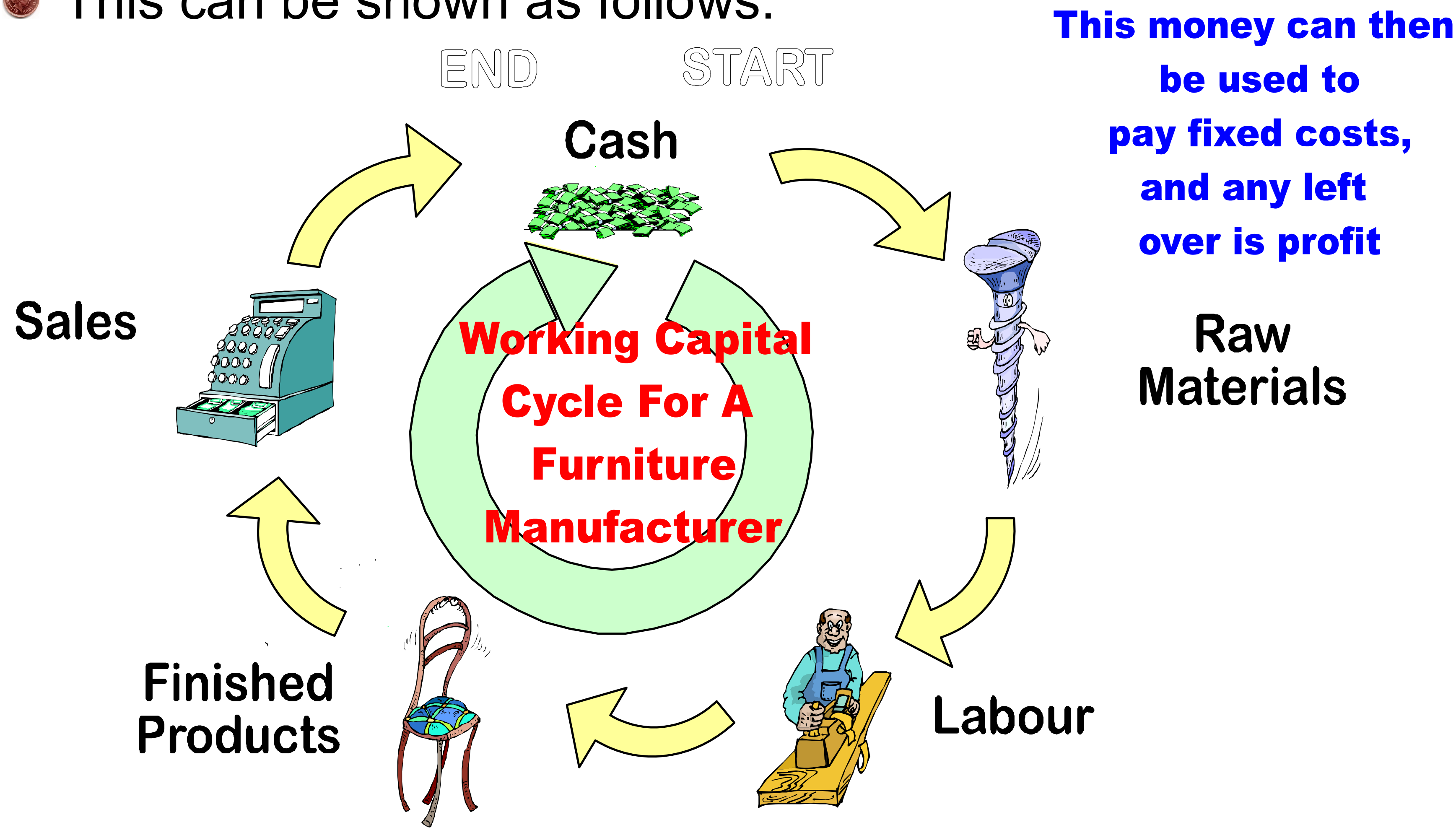
Working Capital

- **Working capital** refers to the materials that a business needs in order to make the products that it sells
- Without working capital a business would be unable to operate
- It is the working capital that produces profit and as such it is referred to as an investment
- However, unlike fixed assets, working capital items are **NOT** intended to be kept by the business

How Money Works In Business

- Money constantly goes round a business in a cycle
- This can be shown as follows:



The Speed of the Working Capital Cycle

- If the amount of cash at the end of the cycle is bigger than that at the start then a firm will make a profit
- How much profit depends upon how quickly they can get round this cycle.
- How quickly it can get round depends on two factors:

Speed of The Working Capital Cycle

Creditors

- People a business owes money to.
- They speed up the cycle

Debtors

- People who owe the business money.
- They slow down the cycle.

Calculating the Working Capital

- The working capital of a firm is calculated as follows:

Working Capital = Current Assets – Current Liabilities

- Where:
  - **Current Assets** =
    - Anything a business owns, which it intends to sell
    - Examples include raw materials, stock, debtors and cash.
  - **Current Liabilities** =
    - Anything that a business owes, which must be paid within the next 12 months
    - Examples include creditors, overdraft and dividends.
- This calculation is part of the **BALANCE SHEET**

Sources of Finance

- Before a business can spend money it must obtain it
- Firms have a number of possible sources of finance:

Sources of Finance

Internal
- Profit
- Depreciation
- Sale of Assets

External

Long Term
- Share Issue
- Mortgage
- Debenture
- Venture Capitalists
- Government Grants

Short Term
- Bank Overdraft
- Bank Loan
- Trade Credit
- Hire Purchase
- Leasing
- Factoring

- Define each source of finance
- Give an example of what each might be used for